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By E-Mail to rule-comments@sec.gov

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OFFICE OF THE SECRETARY

Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549-0609

Re: File No. S7-26-04; Proposed Regulation B

Dear Mr. Katz:

Deutsche Bank AG ("Deutsche Bank") appreciates this opportunity to comment on Release No. 34-49879 (the "Release"), published by the Securities and Exchange Commission (the "Commission") at 69 *Fed. Reg.* 39682, of its proposed Regulation B (the "Proposal"), which would establish the scope of the exemptions for banks from the definition of the term "broker" under Section 3(a)(4) of the Securities Exchange Act of 1934 (the "Exchange Act"), as amended by the Gramm-Leach-Bliley Act ("GLBA").

Deutsche Bank acknowledges and appreciates the Commission's efforts to address the shortcomings in the interim rules adopted in 2001 (Exchange Act Release No. 44291) (the "Interim Rules"). We respectfully submit, however, that the Proposal continues to restrict banks' activities and routine operations, without any commensurate protection to investors, in significant respects; eliminates banks' abilities to provide certain services that banks have traditionally provided and their customers have come to expect; imposes unnecessarily complex requirements on banks that will be extremely difficult and expensive to administer; and puts banks at a significant disadvantage against other non-bank, financial services firms in important respects as well.

The areas of the Proposal that are of particular concern to Deutsche Bank and that we will focus on in the body of this letter can be summarized as follows:

1. The Proposal regulates banks' bonus plans in a manner that is impractical and burdensome to implement and that was neither required nor contemplated by Congress when it enacted the GLBA;

2. The scope of, and the methods of calculation for compliance with, the "chiefly compensated test" under the trust and fiduciary activities exception are overly complex and restrictive;

3. The Proposal prohibits banks from engaging in certain customary and traditional services under the safekeeping and custody exception of the Proposal;

4. The sweep account and the money market exceptions and the definition of "no-load money market fund" are unnecessarily restrictive;

5. The dates used in the grandfathering provisions of the Proposal are impractical; and

6. The Proposal will have unfortunate and unintended consequences unless, prior to the effective date of Regulation B, the NASD revises its Rule 3040 with respect to bank employees who are dual-hatted into a broker dealer.

I. NETWORKING EXCEPTION

The Release specifically requested comments regarding "additional guidance, if any, commenters would find useful with respect to bonus programs." **Release, Section III(A)(2)(b), 69 *Fed. Reg.* at 39690.** Deutsche Bank respectfully submits that the final rule should not incorporate the guidance contained in the Release that would preclude banks seeking to utilize the statutory Networking Exception[1] from awarding discretionary bonuses that are not based solely on the profitability of the bank or bank holding company, because such a requirement would:

(i) Require banks to overhaul their methodology for awarding bonuses to an extent that far exceeds Congress's intent in enacting the GLBA; and

(ii) Deprive banks of the ability to consider as a factor in making bonus awards the contributions of the individual employee, including the employee's impact on the bank's internal controls environment and risk profile.

Although there is nothing in the Proposal itself that refers specifically to bonuses, the Release attempts to "clarify ... the circumstances under which compensation paid in the form of bonuses falls within the networking exception's prohibition on the payment

[1] The Networking Exception in Section 3(a)(4)(b)(i)(VI) of the Exchange Act permits unregistered bank employees to "receive compensation for the referral of any customer if the compensation is a nominal one-time cash fee of a fixed dollar amount . . . ."

of brokerage-related incentive compensation to unregistered bank employees." ***Id.* at 39689.** The release accompanying the Interim Rules equated bonus plans with incentive compensation and stated that unregistered bank employees may not "receive incentive compensation for any brokerage-related activity" other than explicitly permitted referral fees. **66 *Fed. Reg.* at 27766.** In the Release, the Commission noted and specifically rejected comments submitted in response to the Interim Rules that bonus plans should be deemed to be improper incentive compensation only if "used as a conduit to pay brokerage-related compensation to unregistered employees". **69 *Fed. Reg.* at 39690.** The only change made from the Interim Rules is that the Proposal would permit bonuses to be paid based on the overall profitability of the bank holding company **or** the bank, whereas the Interim Rules permitted only bonuses paid based on the overall profitability of the bank.

Many large institutions, including banks, pay discretionary bonuses to their employees. The bonus amounts paid within any specific area of the bank generally are dependent, among other factors, on the profitability of the institution and on the profitability of the specific business line. Typically, an institution allocates a bonus pool to each business line, based on senior management's perception of that business line's overall contributions, and leaves the determination of individual awards from that pool to the management of the business line. In addition, banks, such as Deutsche Bank, will consider various additional factors in determining an employee's bonus amount, including the employee's dedication, work ethics, adherence to the bank's policies, and overall contribution to the goals and success of the institution. The overall bonus award is the product of a wide variety of factors, but, typically, no specific portion of the bonus is tied to referrals or any other objectively determinable criteria.

We respectfully submit that the Commission's interest in preventing evasions of its rule implementing the limitations of the Networking Exception can be achieved without requiring banks either to (i) abandon their existing practice of delegating to the management of the business lines, who are most familiar with the relative contributions of their employees, the task of allocating a bonus pool among individual employees; or (ii) replace their existing qualitative methodologies for calculating bonuses with complex calculations that leave no room to consider individual employees' varying levels of performance. As noted in the comment letters submitted by The Clearing House and the American Bankers Association/ABA Securities Association, Congress, when it enacted the GLBA, did not intend to give the Commission broad authority to so radically change the manner by which banks compensate their employees.

Requiring that bonuses be awarded on the basis of the overall profitability of the bank or bank holding company (and not based on the profitability of the employee's specific branch, department or business line) would also lead to awards being made in lock-step fashion based exclusively on criteria that do not reflect individual accomplishments and contributions. Such a result would not only be impractical, but would also be bad policy, as banks would be discouraged from, for example, increasing the bonuses of employees who have contributed to fostering a strong control environment, or adjusting downward the compensation of employees who have ignored internal controls or recklessly endangered the institution. Such positive or negative contributions may not have any direct impact on the profitability of the bank or bank holding company, but we cannot conceive that the Commission would seek to preclude banks from considering such factors in determining bonus awards.

Accordingly, we respectfully urge the Commission to abandon its requirement that bonuses be awarded solely on the basis of the overall profitability of the bank or bank holding company, and replace it with a standard that simply precludes the specific consideration of referrals to registered brokers or dealers in awarding bonuses.

II. TRUST AND FIDUCIARY ACTIVITIES

A. Chiefly Compensated Requirement

1. Proportion of Sales Compensation Permitted under the Line-of-Business Test

As noted in the Release, the Interim Rules were universally criticized for requiring a complex and burdensome account-by-account determination for purposes of the chiefly compensated test. ***Id.* at 39693-694**. The Proposal provides an alternative line-of-business test that is simpler to administer. However, the line-of-business test is far less flexible in that it permits sales compensation of approximately 10% of relationship compensation, instead of the almost 50% permitted under the account-by-account test.

The Commission Staff has explained that it is concerned that permitting a higher ratio of sales compensation to relationship compensation under the line-of-business test could lead to the abusive practice of using accounts with low ratios of sales compensation to offset true brokerage accounts with extremely high levels of sales compensation. This concern appears to be unfounded, for the following two reasons.

First, this test is relevant only in the context of banks' trust and fiduciary departments where currently most, if not all, accounts are fiduciary in nature and brokerage accounts are not administered out of these departments. Second, proposed Section 242.724(e) defines "line of business" in such a way as to significantly restrict the ability of a bank to combine different types of accounts within a business line that is relying on the trust and fiduciary exception. Consequently, under the Proposal a bank could not administer brokerage and fiduciary accounts within the same department.

Prior to publishing the Proposal, the Commission's staff indicated that the 10% number was chosen to reflect banks' existing levels of securities related business and that the line of business test purposefully does not allow for any growth in this area. Yet, there is no indication in the legislative history that Congress intended to freeze banks' relevant levels of sales compensation at 1999 or 2004 levels. Moreover, as noted above, far less sales compensation is permitted to be received under the line-of-business test than under the account-by-account test.

Consequently, Deutsche Bank endorses the suggestions in the comment letters submitted by The Clearing House (page 15 of its letter dated September 1, 2004) and the American Bankers Association/ABA Securities Association (page 18 of their letter dated September 1, 2004) to increase the ratio of sales compensation that would be permitted under the line-of-business test.

2. Categories of Compensation

Deutsche Bank supports the suggestion in The Clearing House comment letter dated September 1, 2004 (pages 14 to 15), that the Commission simplify the chiefly compensated test by comparing the amount of sales compensation to total compensation, instead of to relationship compensation. This would eliminate the need for banks to categorize and track a third category of "unrelated compensation". It would be much simpler and less expensive to comply with a test with only two categories of compensation. Inasmuch as the Commission's primary concern in proposing limits on sales compensation is the unauthorized or unregulated conduct of brokerage activities within a bank, all compensation not related to brokerage activities, whether currently defined as "relationship" or as "unrelated" compensation, should be outside of the Commission's concern. Such a simplified calculation would provide the Commission with the same level of assurance as the more complex calculation contemplated by the Proposal that banks would not be conducting brokerage businesses contrary to the intent and spirit of the GLBA. For purposes of the remainder of this subsection 2 and in subsection 3 of section III(A) of this letter, we discuss the calculation of the ratio of "sales compensation" to "relationship compensation" consistent with the Proposal.

Deutsche Bank appreciates the Commission's determination that fees paid by mutual fund companies for certain administrative services provided by banks to shareholders (e.g., providing account statements, forwarding communications such as proxies and prospectuses) are exempted from the definition of sales compensation under proposed **Section 242.724(i)(6).** However, the Proposal includes fees paid for these same services in the definition of sales compensation if paid pursuant to a 12b-1 Plan. Banks generally do not control the basis upon which a fund company chooses to pay fees. It is not uncommon for mutual fund companies to compensate banks for administrative services out of their 12b-1 Plans. It should be the purpose of the fees, not their source, that determines whether the fees are sales compensation, and therefore such fees should be excluded from sales compensation so long as they compensate banks for administrative services.

Similarly, compensation a bank receives in connection with client servicing, such as tax preparation, providing assistance with real estate transactions, and similar services, which is currently excluded from the definitions of relationship compensation and sales compensation under **Section 242.724(h) and (i)**, should be treated as relationship compensation. Such compensation is not related to the sales of securities, and therefore raises none of the concerns the Commission is addressing in the Proposal.

3. Waivers of Fees

The Proposal creates a disincentive for a bank to ever grant a customer a waiver of any fee that would be included in relationship compensation. Banks may agree to waive or reduce all or part of an asset-under-management or trustee fee with respect to a particular account for various reasons, including business retention considerations, errors, dispute settlements, or the recognition that another part of the bank may be compensated already in connection with certain investments sponsored or administered by the bank's affiliates. All such fee waivers or fee reductions benefit the customer. In instances where a bank were to make such fee reductions or waivers, the bank would, under the Proposal, not be able to include such reduced or waived fee in its calculation of relationship compensation, thereby increasing the relative amount of its sales compensation, even though the actual ratio of non-brokerage activity to brokerage activity in the account would be unchanged. Accordingly, the bank would risk failing the chiefly compensated test, not because of increased brokerage activity and receipt of additional sales compensation, but because it made a decision to forgo certain non-brokerage-related compensation to which it was otherwise entitled. Consequently, waived fees should be included in relationship compensation for purposes of calculation of the chiefly compensated test.

The Commission suggests that the reason for its proposed approach in excluding waived fees from the computation is to prevent banks from setting unrealistically high administrative fees to comply with the chiefly compensated test with the expectation that such fees would be waived. ***Id.* at 39695.** Bank examiners would easily be able to identify any such potential abuses in the course of their normal reviews. When acting as fiduciaries, banks have an obligation to charge customers reasonable fees in light of the services being provided. Moreover, banks acting as trustees or executors are often subject to statutory requirements and judicial review in charging their fees. If the Commission nevertheless has a continued concern with regard to fee waivers, it would be preferable for the Commission to simply prohibit the practice of setting fees that a bank does not intend to collect, rather than dictating that all waivers adversely affect the bank's ratio of sales compensation.

4. Living, Testamentary or Charitable Trust Accounts

Deutsche Bank believes that the exemption from the chiefly compensated test in the Proposal for banks with existing living, testamentary, or charitable trust accounts should be extended to estates, guardianships and irrevocable trusts. As with living, testamentary, and charitable trusts, banks do not draft governing documents with respect to irrevocable trusts, estates, or guardianships; and, therefore, do not determine the nature of fees to be received in connection with such accounts. Expanding the exception to cover estates, guardianships, and irrevocable trusts is consistent with the Commission's recognition that "banks need flexibility with respect to established personal trust accounts that have terms that cannot be readily changed without consequences to both the bank and the beneficiaries." *Id.* **at 39696.**

B. Scope of the Trust and Fiduciary Activities Exception

In accordance with Exchange Act Section 3(a)(4)(B)(ii), a bank is excepted from the need to register as a broker if it "effects transactions in a trustee capacity, or effects transactions in a fiduciary capacity...." The term "fiduciary capacity" is defined in Section 3(a)(4)(D) as acting as "trustee, executor, administrator, registrar of stocks and bonds, transfer agent, guardian, assignee, receiver, or custodian under a uniform gift to minor act, or as an investment adviser if the bank receives a fee for its investment advice;...[and] in any similar capacity."

In the Release, the Commission specifically requested comment as to whether there are "any capacities similar to the fiduciary capacities listed in the statute in which banks assume fiduciary obligations equivalent to those assumed by banks acting in the listed capacities." *Id.* **at 39701.** One such "similar capacity" is where a bank acts as agent for other trustees. Banks frequently utilize their expertise in providing trust services to act as the agent for others appointed as trustees or as guardians or conservators to assist them in carrying out their fiduciary duties. We wish to emphasize that typically the bank will not have discretion, but, rather, will effect transactions at the actual trustee's direction. In acting as agent in such circumstances, the bank, although not a fiduciary, should nevertheless be deemed to be acting in a "similar capacity" and covered by the trust and fiduciary exception.

C. Investment Advice for a Fee

Exchange Act Section 3(a)(4)(D) defines "fiduciary capacity" to include acting as an "investment adviser if the bank receives a fee for its investment advice." The Proposal states that a bank would be able to rely on the trust and fiduciary activities exception for advisory customers provided that the investment advice includes the "review, selection or recommendation of specific securities...."

Banks, including Deutsche Bank, frequently have arrangements pursuant to which they assist their customers in the selection of third-party advisors, who select or recommend specific securities purchases to the customer. Deutsche Bank believes that its role in assessing the third-party advisors, advising clients in the selection of advisors, and monitoring the appropriateness of such a program for such clients, notwithstanding that it is not selecting or recommending specific securities, should constitute acting in a fiduciary capacity within the scope of Exchange Act Section 3(a)(4)(D). Deutsche Bank is acting as a fiduciary and has a duty to the customers to act with due care in its selection of the advisors, notwithstanding that its advice does not include the review, selection or recommendation of specific securities.

D. Requirement that Activities Be in a Department Regularly Examined by Bank Examiners

The Proposal unnecessarily and inappropriately restricts a bank's reliance on the Trust and Fiduciary Activities Exception to securities transactions by expanding the requirement in Exchange Act Section 3(a)(4)(B)(ii)(I) that such activities must be effected in the bank's "trust department or other department that is regularly examined by bank examiners for compliance with fiduciary principles and standards." According to the Release, "if some aspect of a securities transaction occurs outside of a bank, unless the securities-related activity in question is located within a registered broker-dealer, the bank would be unable to rely upon the trust and fiduciary activities exception for that transaction." ***Id.* at 39704**. The proposed rule is of concern to Deutsche Bank in the context of services outsourced to third parties. Banks are permitted to and typically do outsource a wide variety of functions that may be related to securities transactions, such as routine data processing and similar functions. Under the Proposal it appears that a bank regulatory agency's trust examiners would be required to periodically examine any outsourcing vendor to which even routine functions had been outsourced, despite the fact that the accuracy of the bank's books and records could be verified without recourse to such examination. Such a requirement is contrary to the terms and policies in the Bank Service Company Act, in which Congress explicitly permitted banks to outsource functions subject to a requirement of notification to the appropriate federal bank regulator. 12 U.S.C.§§1861-1864.

III. SAFEKEEPING AND CUSTODY EXCEPTION

Although Deutsche Bank appreciates that the Commission deleted some of the limitations on custody activities contained in the Interim Rules, we believe that the Proposal unnecessarily disrupts banks' traditional custody business by prohibiting order-taking from all custody customers other than qualified investors and accounts established by July 30, 2004.

The Commission proposes to permit banks to take orders only from investors who held custody accounts as of July 30, 2004, or from "qualified investors" as defined in Exchange Act **Section 3(a)(54)**. Accepting orders from investors has always been a customary part of bank custody services. The term "custody and safekeeping" has traditionally been understood to include order taking. Limiting the ability of bank custody departments to carry out orders to purchase and sell securities for certain types of custody customers negates, in Deutsche Bank's view, key aspects of banks' traditional custodial activities and is contrary to the language and intent of the GLBA.

Because many bank custody clients will not meet the "qualified investor" requirement, the Proposal will eliminate the ability of many banks to provide traditional custody services, which include order taking. Further, this prohibition will frustrate the desires of bank clients who choose to utilize the services of a bank custodian instead of a broker, as such investors will be required to either open two accounts - one with a bank and one with a broker-dealer, or move their assets entirely to a broker-dealer. The prohibition on order-taking is particularly troublesome in the context of mutual funds and IRAs.

First, banks should retain the ability to take orders from IRA customers where the bank is not acting as trustee. Banks have provided custodial IRA services, including order-taking, in the 30 years since IRAs were first authorized under the Internal Revenue Code without any demonstrated harm to IRA account holders. These are among the banks' traditional custodial activities that Congress did not intend to disrupt with the enactment of the GLBA. Under the Proposal, a custodial IRA client that wishes to remain a client of the bank would be able to do so only by appointing the bank as trustee. Such appointment, involving a fiduciary responsibility on the part of the bank, would also carry with it higher fees. Yet clients that have self-directed IRAs generally have no need for the services of a corporate trustee and it will not be in their interest to pay higher fees for the sole purpose of retaining a bank as their IRA custodian.

Second, we believe that banks should be able to continue to take orders for mutual funds. Many clients engage in securities activities solely in the context of purchases of mutual fund shares. The Proposal would require such customers to open brokerage accounts solely for the purpose of purchasing mutual fund shares. In addition to limiting a client's right to choose where the client wishes to hold its account, this creates undue expenses for the client. Further, if banks are precluded from taking client orders for mutual funds, their custody businesses will be greatly reduced and, in some cases, they may even be forced out of the custody business altogether.

Even if the Commission is not persuaded by our arguments and continues to believe that order-taking in the custody area should be made available only to investors of certain investment sophistication, Deutsche Bank believes that any perceived risks can be eliminated when banks deal with customers with sophistication of a level less than "qualified investors", such as "accredited investors", as defined in Section 501(a) of the Commission's Regulation D (15 C.F.R. § 230.501(a)).

IV. SWEEP ACCOUNTS

Section 3(a)(4)(B)(v) of the Exchange Act exempts a bank from registering as a broker when it sweeps deposit funds into no-load money market mutual funds. The Proposal adds a further restriction by requiring that not only can there be no front or back-end loads, but charges for sales promotion expense and personal service or the maintenance of shareholder accounts cannot exceed 25 basis points of average net assets. Such a restrictive definition of "no-load" is inconsistent with Congress's intent, and is unnecessary to protect investors as long as fees are properly disclosed, since the Commission agrees that banks' direct charges to clients are not subject to any limit under Regulation B. Forcing banks to charge sweep fees at the account level instead of at the mutual fund level creates an administrative burden without any demonstrable salutary effect on investors.

Accordingly, Deutsche Bank suggests that, even if the Commission declines to revise its definition of "no-load", it nevertheless permit banks to sweep funds into money market mutual funds, whether or not they meet the definition of "no-load", provided that adequate disclosure is provided to customers regarding relevant fee arrangements

In the Proposal, the Commission requested comments on whether rate spread or retained yield fees should be counted as sales charges in determining whether money market funds in a sweep account program involving such fees should be considered "no-load" for purposes of the exception. **69 *Fed. Reg.* 39706**. Since the bank could charge the customer any fee directly, the fact that it charges the same fee by means of a rate spread or retained yield fee should not cause a fund to be regarded as a "load" fund. It would be appropriate for the Commission to require a bank utilizing rate spreads or retained yield fees to provide full and fair disclosure of the practice to the customer.

V. MONEY MARKET MUTUAL FUNDS

Deutsche Bank appreciates the Commission's proposal to exempt a bank from the definition of "broker" when the bank effects transactions for customers in money market mutual funds under specified circumstances. In particular, Deutsche Bank commends the Commission for proposing a rule that is designed to permit banks to continue to perform their traditional corporate trust activities by permitting them to effect transactions in money market mutual funds for customers for which the bank serves as escrow agent, collateral agent, depositary agent, or paying agent. This exemption would be more useful, however, if expanded to permit banks to effect transactions in short-term bond funds that are similar in risk to money market mutual funds.

We also believe that a bank should be permitted to effect transactions in money market mutual funds for a wider range of customers than currently permitted under the Proposal. Under the Proposal, for non-fiduciary and non-corporate trust customers, the bank could effect such transactions only if the customer is a qualified investor. Deutsche Bank believes that the scope of the exemption should be expanded from qualified investors to accredited investors. Given the nature of these investments, we believe that the level of sophistication of accredited investors is sufficient to ensure their protection.

VI. GRANDFATHERING PROVISION

Deutsche Bank is concerned that the grandfathering provisions in proposed **Sections 242.720(a) and 242.760(a)** – relating to the status of living, testamentary or charitable trust accounts under the Trust and Fiduciary Activities Exception and to order-taking under the Safekeeping and Custody Exception, respectively -- create significant record-keeping and operational difficulties, and that instead of grandfathering accounts opened prior to July 30, 2004, the Commission should grandfather accounts opened prior to the effective date of the rules.

Because the rules have not been finalized, and are likely to undergo further modification, it is difficult for banks to determine exactly how to treat accounts opened after July 30, 2004. It would be unfair to custodial customers opening accounts between July 31, 2004, and December 31, 2004, to permit the bank to make accommodation trades through the end of the year, and then terminate these privileges effective January 1, 2005. Accordingly, we believe that a more practical cut-off date would be the effective date of the rules.

Finally, Deutsche Bank requests that the rules should provide that a custody account opened on or before the grandfathering date would not lose its grandfather privileges merely because the bank revises the account documentation at some point in the future, as redocumentation may be required due to proposed **Section 242.762(a)**[2] or for certain other reasons.

VII. NASD Rule 3040

In dialogues with the staff of the Division of Market Regulation, the staff has suggested that many of the apparently paralyzing effects of the Proposal can be mitigated by dual-hatting bank personnel, so that, as registered representatives, they would be eligible to be compensated as brokers. However, it would appear that NASD Rule 3040 would result in a significant increase in the amount of recordkeeping the affiliated broker dealer would be responsible for regarding the dual-hatted employees' activities within and on behalf of the bank. In addition, dual-hatting would entail a dramatic change in the supervisory structure of the bank, as it would entail NASD and Commission review over all activities of the dual-hatted employee within the bank. This has the effect of undermining the concept of functional regulation that is at the core of the amendments to Section 3(a)(4) of the Exchange Act enacted as part of the GLBA. Therefore, we urge the Commission to work with the NASD to ensure that amendments to Rule 3040.are implemented before the effective date of the Proposal so as to avoid such recordkeeping and supervisory burdens.

VIII. CONCLUSION

In summary, we believe that the Proposal is unduly complex and restrictive in the areas described above and that it impacts banks in ways that were not intended by Congress when passing the GLBA. Many of the Proposal's requirements will impose burdens and restrictions, not only on banks, but also on their clients, that were neither foreseen nor intended by Congress. We believe that the goal of strengthening investor

[2] Proposed **Section 242.762(a)** provides that a custody account can be established only pursuant to a "written agreement between the bank and the customer, which provides for the terms that will govern the fees payable, and the rights and obligations of the bank."

protections will not be compromised by the implementation of the changes and revisions that we advocate in this letter. We also generally support, and urge the Commission to give serious consideration to, the comments and recommendations regarding the Proposal that are made in the submissions by the American Bankers Association and The Clearing House Association.

Once again, Deutsche Bank appreciates the opportunity provided by the Commission to comment on the Proposal. We hope that the Commission is persuaded by these comments, but if necessary, we would be happy to provide additional information or clarification.

We thank you for your consideration.

Very truly yours,

Richard H. Walker
General Counsel